

**MINUTES  
REGULAR MEETING  
ARIZONA STATE RETIREMENT SYSTEM BOARD**

**Friday, March 21, 2008  
8:30 a.m., MST**

The Arizona State Retirement System (ASRS) Board met in the 10<sup>th</sup> Floor Board Room, 3300 N. Central Avenue, Phoenix, Arizona. Mr. Michael Townsend, Chair of the ASRS Board, called the meeting to order at 8:37 a.m., MST.

The meeting was teleconferenced to the ASRS office at 7660 E. Broadway, Tucson, Arizona 85710.

**1. Call to Order; Roll Call; Opening Remarks**

Present: Mr. Michael Townsend, Chair  
Dr. Keith Meredith, Vice Chair  
Mr. Dave Byers  
Mr. Tom Connelly  
Mr. Jaime Gutierrez  
Mr. Jim McLaughlin  
Mr. Larry Trachtenberg  
Mr. Steve Zeman

Absent: Mr. Chris Harris

A quorum was present for the purpose of conducting business.

**2. Approval of the Consent Agenda**

**Motion:** Mr. Steve Zeman moved to approve Refunds and Retirements for the month of January, 2008;

*And*

Approve System Transfers for the months of December, 2007 and February, 2008;

*And*

Approve the minutes of the February 15, 2008, Regular and Special Sessions of the ASRS Board.

Mr. Jaime Gutierrez seconded the motion.

By a vote of 8 in favor, 0 opposed, 0 abstentions, and 1 excused, the motion was approved.

**3. Presentation, Discussion and Appropriate Action Regarding 2008 ASRS Legislation**

Mr. Pat Klein, Assistant Director, External Affairs Division, and Ms. Lesli Sorensen, Government Relations Officer, addressed the Board regarding the 2008 ASRS Legislation. Ms. Sorensen gave a brief update highlighting bills of interest.

Mr. Uwe Fink, Legislative Representative, University of Arizona Retiree Association, addressed the Board regarding his concern about current divestment bills. Mr. Fink stated that such bills would have a negative impact on the Fund and that his group has been sending letters to legislators regarding their concern over the issue.

#### **4. Presentation, Discussion and Appropriate Action Regarding Investment Industry Update, Investment Industry Trends and Implications for the ASRS**

Mr. Terry Dennison presented an investment industry trends update to the Board. Mr. Dennison provided a comprehensive presentation regarding general investment trends as well as trends that may specifically apply to or affect the ASRS. Mr. Dennison answered questions from Trustees regarding the presentation.

Mr. Tom Connelly requested another presentation that would define what constitutes an asset class and what constitutes a source of beta. Mr. Connelly suggested that this may occur either at a future Investment Committee meeting or at a future Board meeting.

#### **5. Presentation, Discussion and Appropriate Action Regarding Global Tactical Asset Allocation (GTAA) Manager(s) Search**

Mr. Gary Dokes, Chief Investment Officer, Mr. Dan Kapanak, Manager of Investment Strategies and Mr. Terry Dennison, Worldwide Partner, Mercer Consulting, addressed the Board regarding the Global Tactical Asset Allocation Manager(s) search. Mr. Dokes stated that the ASRS terminated GTAA manager Goldman Sachs Asset Management (GSAM) in 2007, as the result of organizational, investment process, and performance concerns. GSAM's assets of approximately \$1.4 billion were transferred to Bridgewater, ASRS existing GTAA manager (\$400 million), and BGI (\$1 billion). BGI was to manage the assets passively consistent with the ASRS strategic policy benchmark until one or more active GTAA replacement managers were approved for hiring.

Given the ASRS preference to hire GTAA managers who generate alpha primarily by tactically over- and under-weighting asset classes consistent with those in the ASRS strategic asset allocation policy, the search was revised to identify GTAA managers who have the expertise and willingness to manage a GTAA mandate based on the ASRS' individual benchmark and GTAA constraints. The seven short-listed candidates and three additional candidates were contacted to discuss a customized GTAA implementation.

An ASRS GTAA Search Committee (Committee) consisting of an IC member, Director, CIO, IMD staff, and Mercer (general and GTAA specialist) reviewed the material provided by the candidates and Mercer. Based on the quality criteria of asset management, performance details, risk and return characteristics, ability to implement the customized GTAA strategy, and fee structure, the Committee prepared a finalist list of investment managers.

In January, three finalists were interviewed by the Committee. Based on the managers' presentations, responses to questions from the Committee, and discussions among Committee members, Deutsche Asset Management and Mellon Capital Management were selected for hire based on the expectation that both managers will add alpha relative to ASRS benchmark, and the diversification benefits of the investment process and styles between Deutsche and Mellon and Bridgewater, the incumbent ASRS GTAA managers.

Mr. Dokes stated that recent information provided by Mercer regarding Mellon Capital Management has altered the original recommendation. Further research into Mellon Capital Management will be necessary before moving forward with that manager. Presently, the recommendation to hire Deutsche Asset Management stands, but Mellon Capital Management will be revisited in the near future.

**Motion:** Mr. Larry Trachtenberg moved to hire Deutsche Asset Management as an ASRS GTAA Manager;

*And*

To fund Deutsche Asset Management with approximately \$500 million from the GBI GTAA passive portfolio.

Mr. Jim McLaughlin seconded the motion.

By a vote of 8 in favor, 0 opposed, 0 abstentions, and 1 excused, the motion was approved

#### **6. Presentation, Discussion and Appropriate Action Regarding BlackRock Financial Management's Mortgage Investors Fund**

Mr. Gary Dokes, Mr. Brian Luedtke, Fixed Income Portfolio Manager and Mr. Terry Dennison addressed the Board regarding BlackRock Financial Management's Mortgage Investors Fund. Mr. Dokes stated that given the occurrence of the dislocation in the fixed income and real estate mortgage securities markets, tactical investment opportunities appear to exist and continue to develop that are expected to provide investors with an attractive risk/return investment profile environment in which to invest. The market volatility caused by the distressed mortgage securities markets has led to the availability of Residential Mortgage Backed Securities (RMBS), Commercial Mortgage Backed Securities (CMBS) and other mortgage debt securities at attractive discounted market prices relative to their perceived economic underlying asset values.

The BlackRock Mortgage Investors Fund was created to capitalize on this opportunistic, short-to-intermediate market dislocation. Blackrock intends over the next couple years to purchase high quality securitized cusip-level bonds as distressed sellers de-lever balance sheets and reduce exposure to this market segment. Blackrock foresees a final portfolio consisting of approximately 1/3 securities backed by commercial mortgages and 2/3 securities backed by residential mortgages. However, due to the opportunistic nature of this fund, the final composition of the fund may vary from the original estimates.

Due diligence was conducted by the ASRS Investment Management Division (IMD) staff, Townsend Partners (ASRS real estate consultant) and Mercer (ASRS general consultant) and provides an effective check-and-balance tool within ASRS investing decision-making process.

At the most recent Real Estate Committee (REC) meeting, Committee members and Townsend consultants (including their real estate debt specialist) discussed the merits of the BlackRock Fund. Though a consensus exists that tactical opportunities will be available in the distressed real estate mortgage market, the REC voted not to consider the Fund for the ASRS real estate program because the ASRS real estate program has to date only considered equity or commercial investments and not investments with fixed income attributes.

The BlackRock Mortgage Investors Fund will be considered an Opportunistic Asset Class given the tactical nature of the investment. Per the ASRS Strategic Asset Allocation Policy, Opportunistic Asset Classes include investment opportunities that do not fall into clearly-defined asset classes, take advantage of changing and tactical market conditions or are driven by perceived changes in the relative values of various asset classes.

**Motion:** Mr. Larry Trachtenberg moved to invest \$75 million in the BlackRock Mortgage Investors Fund; funding from BGI's Enhanced U.S. Debt Index Fund;

*And*

To classify and report the BlackRock Mortgage Investors Fund as an Opportunistic Asset Class within ASRS Asset Allocation Policy.

Mr. Steve Zeman seconded the motion.

By a vote of 8 in favor, 0 opposed, 0 abstentions, and 1 excused, the motion was approved.

## **7. Presentation, Discussion and Appropriate Action Regarding the ASRS Strategic Plan**

Mr. Paul Matson, Director, Mr. Anthony Guarino, Deputy Director and Ms. Sara Orozco, Strategic Planning Manager, addressed the Board regarding the ASRS Strategic Plan. Mr. Guarino stated that the ASRS is proceeding as expected toward achieving the goals and objectives it set for the three-year period ending December 2008. The agency employs a strategic model that assumes goals can be met by focusing attention on sound governance policy, management and measurement of performance, relevant strategic initiatives and sensible budgeting that includes investment in human resources.

Mr. Guarino stated the ASRS believes that implementing sound governance policies creates the necessary internal environment to effectively achieve agency goals and other strategic aims (vision, values, statutory purpose, and investment principles). In addition to delineating duties and responsibilities, the ASRS Governance Handbook details agency oversight structures, reporting requirements and other activities needed to facilitate strategic thinking and acting.

Operating within the organizational framework set up through its Governance Handbook, each of the three ASRS divisions (Operations, Investments, External Affairs), led by the Director and Board, is moving to achieve the numerous business objectives articulated in the plan. These objectives represent

both qualitative and quantitative standards of performance excellence the agency expects to achieve by December 2008, and are directly linked to its fourteen strategic goals.

A number of key initiatives were completed in 2007, such as a review and analysis of the ASRS Plan Design, continued implementation of systems and processes designed to improve service and performance, improvement of data integrity of member accounts, and development of a brand of service that is reflective of the agency's values.

Ms. Sara Orozco reviewed the proposed changes to the Strategic Plan and provided a thorough update of achievements to the Trustees.

Mr. Jaime Gutierrez excused himself from the meeting at 10:44 a.m.

**Motion:** Mr. Steve Zeman moved to accept the report and recommend modifications to the ASRS Strategic Plan as noted in the March 21, 2008, ASRS Board meeting.

Mr. Dave Byers seconded the motion.

By a vote of 7 in favor, 0 opposed, 0 abstentions, and 2 excused, the motion was approved.

## **8. Director's Report**

Mr. Paul Matson informed the Trustees that updated 2008 Strategic Initiatives were included in the Director's Report section of the Board book for their review.

## **9. Possible Presentation Regarding Board Committee Updates**

Mr. Steve Zeman, Vice Chair, External Affairs Committee (EAC), stated that the next EAC meeting would be in early April.

Mr. Larry Trachtenberg, Chair, Investment Committee (IC), said an IC meeting has been scheduled for early April.

Mr. Dave Byers, Chair, Operations Committee (OC), stated that the next OC meeting would be the third Thursday in April.

## **10. Board Requests for Agenda Items**

There were no requests for agenda items.

## **11. Call to the Public**

Ms. Pat Mitkos, ASRS Member, addressed the Board regarding a concern she has about her years of service. Ms. Mitkos stated that the ASRS has the wrong years of service on record for her and that she would like this corrected. Mr. Michael Townsend instructed staff to work with Ms. Mitkos regarding the issue.

**12. The next ASRS Regular Board meeting is scheduled for Friday, April 18, 2008, at 8:30 a.m., at 3300 N. Central Avenue, 10<sup>th</sup> Floor Board room, Phoenix, Arizona.**

**13. Adjournment of the ASRS Board**

Mr. Townsend adjourned the March 21, 2007 Board meeting at 11:15 a.m.

ARIZONA STATE RETIREMENT SYSTEM

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Anne Schrode, Secretary

Date

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Paul Matson, Director

Date